

# Kansas City Life Insurance Company

## 2012 Second Quarter Report



*Includes our subsidiaries:*

Sunset Life Insurance Company of America  
Old American Insurance Company  
Sunset Financial Services, Inc.

Post Office Box 219139  
Kansas City, Missouri 64121-9139  
Listing: NASDAQ  
Stock Symbol:KCLI  
[www.kclife.com](http://www.kclife.com)



# *Message* from the President, CEO and Chairman of the Board

Kansas City Life Insurance Company recorded net income of \$8.4 million or \$0.78 per share in the second quarter of 2012, a \$2.8 million or \$0.19 per share decrease relative to the same quarter in the prior year. Insurance revenues improved \$5.2 million or 10% for the period, but this was offset by \$6.8 million in increased policyholder benefits and amortization of deferred policy acquisition costs. In addition, investment revenues declined \$2.0 million or 4%, negatively impacting earnings for the second quarter relative to the prior year.

Net income for the first six months of 2012 was \$27.8 million or \$2.50 per share, an improvement of \$11.9 million or \$1.11 per share over the prior year results. This increase was largely the result of net realized investment gains of \$16.9 million in the first half of 2012, rising \$14.4 million over the first six months of 2011. Also contributing to the improved year-to-date earnings were increased insurance revenues and declines in policyholder benefits and operating expenses.

Insurance revenues increased \$5.2 million or 10% in the second quarter of 2012. This increase was largely the result of a \$2.6 million increase in new premiums, driven by \$2.4 million in increased immediate annuity sales, and a \$1.8 million increase in contract charges. The increase in contract charges was largely the result of an unlocking of assumptions that impacted the amortization of deferred revenue from selected universal life-type products.

Insurance revenues increased \$3.2 million or 3% in the first six months of 2012, primarily due to a \$1.4 million increase in new immediate annuity receipts, a \$1.4 million increase in renewal premiums on traditional life insurance products, and a \$0.7 million increase in contract charges.

Continued low interest rates and the uncertain economic environment negatively impacted new sales of deposit products, including an \$8.1 million or 29% decline in new interest sensitive products in the second quarter versus one year earlier. This included reductions in new universal life deposits of \$0.9 million or 24% and new fixed deferred annuities of \$5.6 million or 31%. In addition, new variable universal life and annuity deposits declined \$1.7 million or 26% in the second quarter. New deposits decreased \$3.3 million or 7% in the six months versus the prior year, including a \$1.3 million or 4% decrease in new fixed deferred annuities and a \$1.6 million or a 15% decrease in variable life and annuity products.

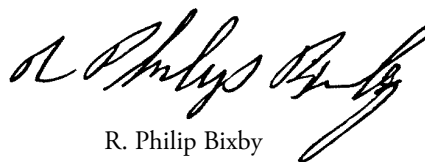


Total investment revenues, including net investment income and net realized investment gains and losses, decreased \$2.0 million or 4% in the second quarter compared with the same period in the prior year. This decrease was the result of \$1.5 million in reduced net investment income and a \$0.5 million decrease in net realized investment gains. Total investment revenues increased \$11.7 million in the first six months over the prior year. This increase was the result of \$16.2 million in gains on real estate sales, primarily generated in the first quarter of 2012. Net investment income declined \$2.6 million or 3% for the six months versus the prior year. The reduced net investment income in both periods was largely due to lower yields on the Company's primarily fixed-rate investment portfolio.

Policyholder benefits increased \$2.4 million or 6% for the second quarter of 2012 compared with the same period one year earlier. This was largely the result of an increase in benefit and contract reserves, reflecting the growth in new immediate annuity receipts and the increased value of policy riders with guaranteed withdrawal benefits. Policyholder benefits decreased \$4.4 million or 5% for the six months of 2012 versus the prior period. This decrease reflected favorable mortality, as death benefits declined, along with a reduction in group dental benefits paid, and increased reinsurance of group accident and health products.

The amortization of deferred acquisition costs (DAC) increased \$4.4 million in the second quarter of 2012 and \$2.7 million for the six months compared to the same periods one year earlier. These increases were largely the result of favorable unlocking of policy assumptions in the second quarter of 2011, which decreased the amortization of DAC in both the second quarter and first six months of last year.

On July 23, 2012, the Kansas City Life Board of Directors declared a quarterly dividend of \$0.27 per share that will be paid on August 8, 2012 to stockholders of record on August 2, 2012.

  
R. Philip Bixby



**KANSAS CITY LIFE INSURANCE COMPANY**  
**CONSOLIDATED BALANCE SHEETS**

(amounts in thousands, except share data)

	<u>June 30</u> 2012	<u>December 31</u> 2011
<b>ASSETS</b>	(Unaudited)	
Investments:		
Fixed maturity securities available for sale, at fair value	\$ 2,816,250	\$ 2,682,142
Equity securities available for sale, at fair value	37,184	36,689
Mortgage loans	579,500	601,923
Real estate	123,450	127,962
Policy loans	79,447	80,375
Short-term investments	17,448	49,316
Other investments	2,865	3,364
Total investments	<u>3,656,144</u>	<u>3,581,771</u>
Cash	5,573	10,436
Accrued investment income	35,784	34,705
Deferred acquisition costs	178,911	181,564
Reinsurance receivables	194,028	189,885
Property and equipment	22,178	22,671
Other assets	51,180	60,601
Separate account assets	320,566	316,609
Total assets	<u>\$ 4,464,364</u>	<u>\$ 4,398,242</u>
 <b>LIABILITIES</b>		
Future policy benefits	\$ 886,077	\$ 879,015
Policyholder account balances	2,114,159	2,089,452
Policy and contract claims	32,152	36,511
Other policyholder funds	152,124	152,125
Other liabilities	222,254	213,825
Separate account liabilities	320,566	316,609
Total liabilities	<u>3,727,332</u>	<u>3,687,537</u>
 <b>STOCKHOLDERS' EQUITY</b>		
Common stock, par value \$1.25 per share		
Authorized 36,000,000 shares,		
issued 18,496,680 shares	23,121	23,121
Additional paid in capital	41,106	41,101
Retained earnings	802,652	780,918
Accumulated other comprehensive income	42,916	30,086
Treasury stock, at cost (2012 - 7,439,747 shares;		
2011 - 7,187,315 shares)	<u>(172,763)</u>	<u>(164,521)</u>
Total stockholders' equity	<u>737,032</u>	<u>710,705</u>
 Total liabilities and stockholders' equity	<u>\$ 4,464,364</u>	<u>\$ 4,398,242</u>

*Please refer to the Company's Form 10-Q and Annual Report on Form 10-K.*



**KANSAS CITY LIFE INSURANCE COMPANY**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(amounts in thousands, except share data)

	Quarter Ended June 30		Six Months Ended June 30	
	2012	2011	2012	2011
	(Unaudited)		(Unaudited)	
<b>REVENUES</b>				
Insurance revenues:				
Premiums, net	\$ 34,205	\$ 30,801	\$ 66,909	\$ 64,426
Contract charges	25,590	23,752	50,723	49,986
Total insurance revenues	<u>59,795</u>	<u>54,553</u>	<u>117,632</u>	<u>114,412</u>
Investment revenues:				
Net investment income	43,435	44,893	87,644	90,284
Net realized investment gains, excluding impairment losses	1,361	1,893	17,198	2,905
Net impairment losses recognized in earnings:				
Total other-than-temporary impairment losses	(188)	(238)	(456)	(507)
Portion of impairment losses recognized in other comprehensive income	42	56	150	114
Net impairment losses recognized in earnings	<u>(146)</u>	<u>(182)</u>	<u>(306)</u>	<u>(393)</u>
Total investment revenues	<u>44,650</u>	<u>46,604</u>	<u>104,536</u>	<u>92,796</u>
Other revenues	<u>2,312</u>	<u>2,666</u>	<u>4,497</u>	<u>5,074</u>
Total revenues	<u>106,757</u>	<u>103,823</u>	<u>226,665</u>	<u>212,282</u>
<b>BENEFITS AND EXPENSES</b>				
Policyholder benefits	41,276	38,865	79,746	84,139
Interest credited to policyholder account balances	20,377	20,766	40,935	41,247
Amortization of deferred acquisition costs	5,121	705	13,022	10,289
Operating expenses	<u>27,078</u>	<u>26,498</u>	<u>51,040</u>	<u>52,363</u>
Total benefits and expenses	<u>93,852</u>	<u>86,834</u>	<u>184,743</u>	<u>188,038</u>
Income before income tax expense	12,905	16,989	41,922	24,244
Income tax expense	<u>4,508</u>	<u>5,816</u>	<u>14,084</u>	<u>8,280</u>
<b>NET INCOME</b>	<u>\$ 8,397</u>	<u>\$ 11,173</u>	<u>\$ 27,838</u>	<u>\$ 15,964</u>
<b>COMPREHENSIVE INCOME, NET OF TAXES</b>				
Change in net unrealized gains on securities available for sale				
	\$ 15,925	\$ 19,802	\$ 18,017	\$ 19,178
Change in future policy benefits	(3,502)	(2,926)	(4,969)	(2,206)
Change in policyholder account balances	<u>(143)</u>	<u>(83)</u>	<u>(218)</u>	<u>(77)</u>
Other comprehensive income	<u>12,280</u>	<u>16,793</u>	<u>12,830</u>	<u>16,895</u>
<b>COMPREHENSIVE INCOME</b>	<u>\$ 20,677</u>	<u>\$ 27,966</u>	<u>\$ 40,668</u>	<u>\$ 32,859</u>
Basic and diluted earnings per share:				
Net income	<u>\$ 0.78</u>	<u>\$ 0.97</u>	<u>\$ 2.50</u>	<u>\$ 1.39</u>

*Please refer to the Company's Form 10-Q and Annual Report on Form 10-K.*

